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# **Family Policy in Hungary**

**HOW TO IMPROVE THE RECONCILIATION  
BETWEEN WORK AND FAMILY?**

**Philip Hemmings**

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**ECONOMICS DEPARTMENT WORKING PAPERS No. 566**

by  
**Philip Hemmings**

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## ABSTRACT/RESUMÉ

### **Family policy in Hungary: how to improve the reconciliation between work and family?**

Hungarian family policy focuses on providing generous options to take time off work to look after children. This system not only contributes to Hungary's low employment rate but encourages long separation from the labour market, has largely failed to significantly influence fertility rates and is relatively expensive to run. This paper looks at how to shift the policy focus towards reconciling work and family life. Reasons for under-provision in childcare by local governments are discussed and recommendations for further central-government intervention to improve supply are made. Recommendations for reform are also made regarding the complex system of family cash benefits and leave allowances.

This Working Paper relates to the 2007 *OECD Economic Survey of Hungary* ([www.oecd.org/eco/surveys/hungary](http://www.oecd.org/eco/surveys/hungary)).

*JEL classification:* H31, H53, I38, J13.

*Key words:* Hungarian, Hungary, family policy, family benefits, childcare, fertility

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### **La politique familiale en Hongrie : comment mieux concilier travail et vie de famille**

En Hongrie, la politique familiale consiste surtout en larges facilités de congé pour l'éducation des enfants. Cette politique ne se traduit pas seulement par un faible taux d'emploi ; elle a aussi favorisé de longues périodes d'inactivité tout en échouant largement dans son objectif de plus forte fécondité et en étant relativement coûteuse. On examinera dans ce document comment réorienter ces mesures d'une façon qui permette de mieux concilier travail et vie de famille. On verra pourquoi les services d'accueil de l'enfance sont insuffisants au niveau des collectivités locales et on recommandera de nouvelles initiatives de l'administration centrale pour développer ces services. On préconisera également une série de réformes du système complexe de prestations familiales en espèces et d'allocations pour congés.

Ce document de travail se rapporte à *l'Etude économique de l'OCDE de la Hongrie 2007* ([www.oecd.org/eco/etudes/hongrie](http://www.oecd.org/eco/etudes/hongrie)).

*Classification JEL:* H31, H53, I38, J13.

*Mots clés:* Hongrois, Hongrie, politique de la famille, prestations familiales, accueil de l'enfance, fécondité

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## TABLE OF CONTENTS

FAMILY POLICY IN HUNGARY: HOW TO IMPROVE THE RECONCILIATION BETWEEN WORK AND FAMILY? .....	5
Families in Hungary: some basic facts .....	6
Key features of family support .....	8
Long-term financial support .....	8
Additional financial support for the first years of parenthood .....	9
Non-financial support .....	9
Policy needs to focus more on reconciliation between work and family life .....	11
Promoting flexible supply responses in public childcare .....	12
Improving the system of initial financial support and leave allowances .....	14
Dealing with welfare traps .....	15
Avenues for further simplification .....	17
Encouraging the creation of family-friendly jobs and work environments .....	17
BIBLIOGRAPHY .....	19
ANNEX A1 DETAILS OF FAMILY SUPPORT <sup>1</sup> .....	20
ANNEX A2 THE INFLUENCE OF CASH BENEFITS ON FAMILY INCOME .....	23
ANNEX A3 IMPACT OF THE JANUARY 2006 CHANGES TO FINANCIAL SUPPORT FOR FAMILIES .....	25

### Figures

4.1. Key features of families in Hungary .....	7
4.2. International comparison of the duration of paid maternity and parental leave .....	9
4.3. Inactivity rates of mothers by the number of children .....	10
4.4. International comparison of expenditure on family support .....	12
4.5. The welfare trap problem .....	15
4.A2.1. Family incomes: some illustrative scenarios .....	24

### Boxes

Box 1. Key recommendations on family policy .....	5
Box 2. Recent research on the influences on fertility .....	12
Box 3. The debate about east-European equivalence scales .....	16



## FAMILY POLICY IN HUNGARY: HOW TO IMPROVE THE RECONCILIATION BETWEEN WORK AND FAMILY?

by  
Philip Hemmings<sup>1</sup>

Hungarian family policy faces significant challenges in improving the reconciliation between work and family life. The current system focuses on providing generous options for women to take time off work and look after children on a full time basis. In the context of raising the aggregate employment rate, this issue is not as significant as problems relating to disability and early retirement pensions. However, the long separations from the labour market that the system encourages have downsides for women's careers. Also, claims of significant positive effects on fertility are questionable and the system involves relatively high levels of public spending. The paper first looks at trends in the number and composition of families and then describes the various forms of financial and in-kind family support. This is followed by an assessment of current policy and detailed recommendations on how the system could be reformed (these are summarised in Box 1 below).

### Box 1. Key recommendations on family policy

The most immediate barrier to better reconciliation of work and family life is under-provision of childcare services which, for example, arises from externalities in human capital development and social cohesion. The following measures should be considered:

- Continued attention to provision requirements. The impact of the changes in provision regulations should be closely monitored and, if necessary, bolstered by further measures. In terms of service flexibility, policy goals laid out in the government's programme, *New Hungary*, should be followed up. In particular, plans to encourage longer operating hours of childcare facilities look promising.
- Reduction in the municipalities' contribution to costs. Further increases in the central-government grant for services could be useful, as long as savings can be found elsewhere in the system – reductions in family cash benefits is one candidate. The restrictions on parental fees could also be lightened.

1. Philip Hemmings is a staff economist at the OECD. This paper first appeared as a chapter for the OECD *Economic Survey of Hungary*, published in May 2007 under the responsibility of the Economic and Development Review Committee. The author would like to thank OECD colleagues Willem Adema, Andrew Dean, Alessandro Goglio, Val Koromzay, Mark Pearson, and Andreas Woergoetter for their comments as well as Margaret Morgan for statistical assistance. Expert advice was also provided by Hungarian officials, particularly Dora Benedek, Reka Firle, Maria Korodi and Agota Scharle at the Ministry of Finance and Zsafia Toth at the Ministry of Social Affairs and Labour.

- New funding arrangements. A system in which vouchers are given to parents to spend on childcare services (possibly in lieu of cash benefit) could be one way of widening provision and allowing subsidies to more strongly reflect parental preferences.

Assessment of the system of cash benefits for families and leave options suggests reforms should be considered that contain the following elements:

- Removal of the universal third-child benefit and significant reform of the benefits for when children are below kindergarten age. Whatever specific changes are considered, possibilities for extended leave ought to be cut back and savings in spending made to help fund childcare services. Some offset could be made through increases in the replacement rate (and perhaps raising of the cap) of the insurance benefit covering standard maternity leave. Increased paternity leave should also be considered.
- Further simplification of the system. Three schemes could be removed without any significant implications for either the universal or targeted “safety net” dimensions of policy. The cash component of the “child social support” is effectively redundant due to the new welfare top-up payments. Also, the maternity grant and the third-child tax allowance provide relatively small cash support that could be integrated into another benefit, such as the family allowance.
- Removal of welfare-traps. Changes to the equivalence scale used in calculating the welfare top-up payments should be considered. Additional measures could comprise extension of the period allowing retention of a share of the welfare top-up payments, or the introduction of earned-income tax credits.

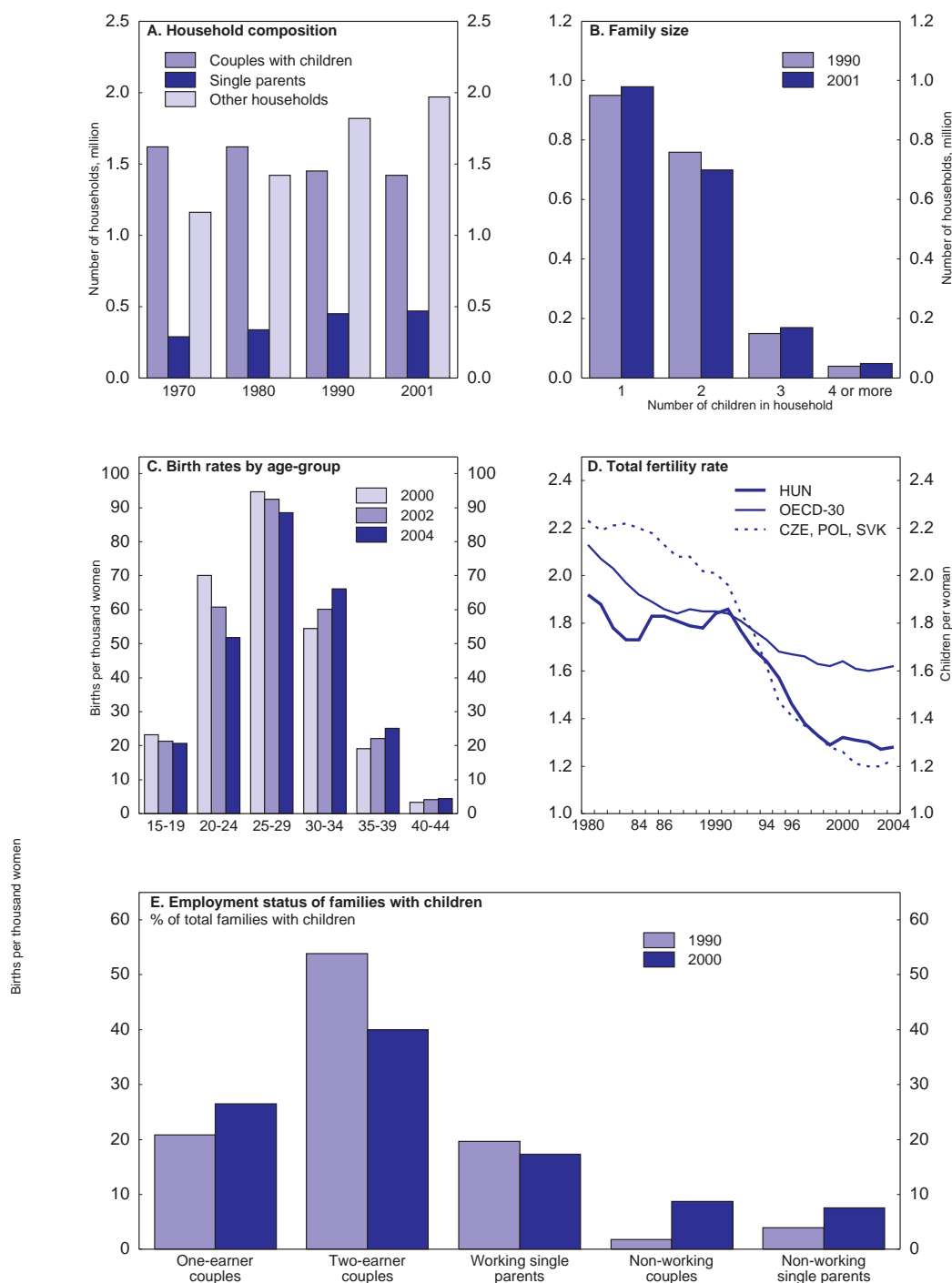
Further work is needed to identify and remove any barriers to the creation of jobs with hours and flexibility that suit working parents. Further reforms that give more flexible choices to public-sector employees would provide a useful lead on this front. Also, when room becomes available to proceed with tax reductions, resumption of the phase out of the lump-sum employers’ healthcare contribution ought to be on the priority list.

### **Families in Hungary: some basic facts**

Family policy affects a large share of the population. Households with children represent about half of Hungary’s 4 million households (Figure 1). Furthermore, even among the growing number of households without children, family policy is often relevant, either because of family ties or because children are planned at some point in the future. As elsewhere, single-parent families are now relatively common. Indeed, about one quarter of households with children are headed by single parents.

The shift towards starting families later is still under way. For instance, as shown in Figure 1 even since 2000 there have been large changes in birth rates in specific age groups. The birth rate among women aged 20-24 fell substantially between 2000 and 2004 whilst the rates among 30 to 34 and 35 to 39 year olds rose. These figures largely reflect women starting families later (the postponement process), which has been a major factor driving the fall in the total fertility rate (Figure 1). Though fertility is expected to start rising in the coming years as the postponement process works through, the pace of increase is uncertain and the eventual “steady state” is likely to be below pre-postponement fertility levels. For a start, postponement means an increased chance that ambitions to have children will be unfulfilled. Furthermore, past trends probably reflect more than just postponement, with increasing numbers of women planning never to have children or, if they do, to have fewer than previous generations.<sup>2</sup>

2. Demographic projections produced for the Hungarian Central Statistical Office (Habcsek, 2006) have a baseline where total fertility rises and then stabilises at 1.5 from 2020 onwards and two variants in which fertility remains roughly constant at 1.3 and where it stabilises at 1.8 from 2025 onwards. These figures suggest that, at best, the recovery in fertility will indeed be below that required to maintain population constant (abstracting from the effects of net migration and increases in life expectancy).

Figure 1. Key features of families in Hungary<sup>1</sup>

1. The total fertility rate is the expected number of children that would be born per woman, in her child-bearing years (15 to 49), based on current age-specific fertility rate data. A total fertility rate of 2.1 children per woman ensures broad stability of the population, on the assumptions of no migration flows and unchanged mortality rates. Rates for regions are averages of country rates.

Source: Hungarian Central Statistical Office; OECD, *Society at a Glance*, 2006.



The changing fertility patterns are affecting the size of families. Comparing census results for 1990 and 2001, the number of households with one child has been increasing while the number of two-child households has fallen (Figure 1). Some of this reflects growth in the number of women who, by either choice or circumstance, only have one child. But such shifts can also be temporary, caused by changing fertility patterns such as postponement. The number of households with three or more children is relatively low; totalling less than 20 000 compared with about 170 000 households with one or two children. The slight increase in households with three children shown in Figure 1 possibly reflects the effects of several explicit incentives to have a third child.

In terms of family working arrangements, two-earner couples remain the most common, accounting for around 40% of households with children (Figure 1). However, the share of two-earner families has fallen since the early 1990s due to increasing numbers of single-earner couples as well as non-working couples and single parents. Much of this is due to economic developments. The restructuring of industry in the 1990s has resulted in high levels of structural unemployment (and low employment rates). This has affected the number of earners within families and contributed to weak female labour supply. Indeed, econometric analysis has found female labour-market participation to be strongly influenced by local unemployment rates (Scharle, 2007).

### **Key features of family support**

Hungarian family support can be grouped into long-term financial support, additional financial support for the first years of parenthood and non-financial support. Full details of the schemes are shown in Annex A1 and scenarios illustrating how the system of cash benefits works are shown in Annex A2.

#### ***Long-term financial support***

The most important universal long term support comes from family allowances. The per-child allocations increase with the number of children (up to the third child) and are higher for single-parent households. From January 2006, more long-term financial support has been channelled *via* family allowances. The per-child allocations were raised while a 13<sup>th</sup> month family allowance payment was scrapped, tax credits were cut back (there is now only a credit for a third child) and monthly means-tested social support for children was reduced to two small biannual payments. These changes aimed at simplifying the system rather than changing the total level of support to families (see Annex A3).

A system of welfare top-up payments (the “guaranteed social minimum”, Rendszeres szociális segély), introduced in June 2006, is now the main element of targeted support to low-income households (with or without children). The top-up covers any gap between reported income and the guaranteed social minimum, which is a multiple of the minimum pension based on family size (see Annex A1). The applicant must be non-employed and typically must agree to engage in certain activation measures to be eligible for benefit. Prior to the introduction of this system safety-net provision was more piecemeal, comprising social security payments for parents and a separate scheme of “child protection support” (which, as discussed above, has been cut back) plus whatever universal benefits the family was eligible for.

Housing support schemes provide implicit support for families because the means tests for eligibility are based on household size. The schemes are administered by local authorities and take the form of cash payments and free, or heavily subsidised, rental accommodation.

### *Additional financial support for the first years of parenthood*

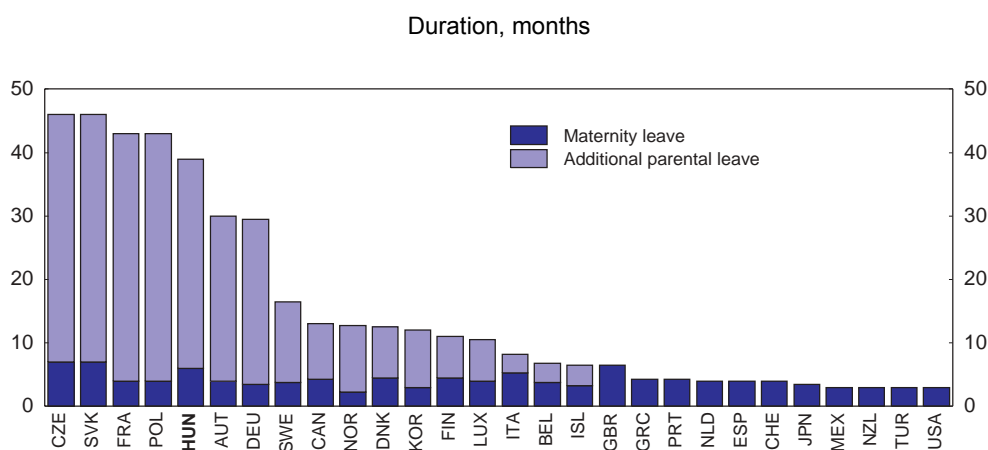
A universal one-off payment is provided at the birth of each child (the “maternity grant”), though this is relatively small in value compared with the other benefits. One scheme, GYES, is available to all families with children aged under three and benefit can be extended beyond age three when there is a third child under a follow-up scheme (GYET). Women covered by social insurance can claim more generous benefits under two schemes: TGYAS, an earnings-related benefit that spans maternity leave and GYED, which is also earnings-related and can last until the child is two years old.

A welcome and potentially important change to the GYES scheme has been made. From early 2006 women have been able to receive GYES while working full time once their child is one year old. Previously, women could only work up to 20 hours per week and be eligible for benefit. Given the small market for part-time jobs in Hungary, the former provision was probably little used. Therefore, it is possible that the relaxation of the rules is bringing about a significant increase in the number of women choosing to work while their children are pre-kindergarten age. However, experts generally agree that it is too early to gauge impact of this change.

### *Non-financial support*

Leave options are generous. The maternity leave allowance is six months. However, being on GYES necessarily involves leave and claimants to GYED have entitlement to leave (claimants to the GYET benefit for third children however forfeit any entitlement to return to their previous employer). In most cases these benefits are claimed by the mother, therefore extending leave entitlement up to three years for each child. This is long compared with most other OECD countries (Figure 2).

Figure 2. International comparison of the duration of paid maternity and parental leave<sup>1</sup>

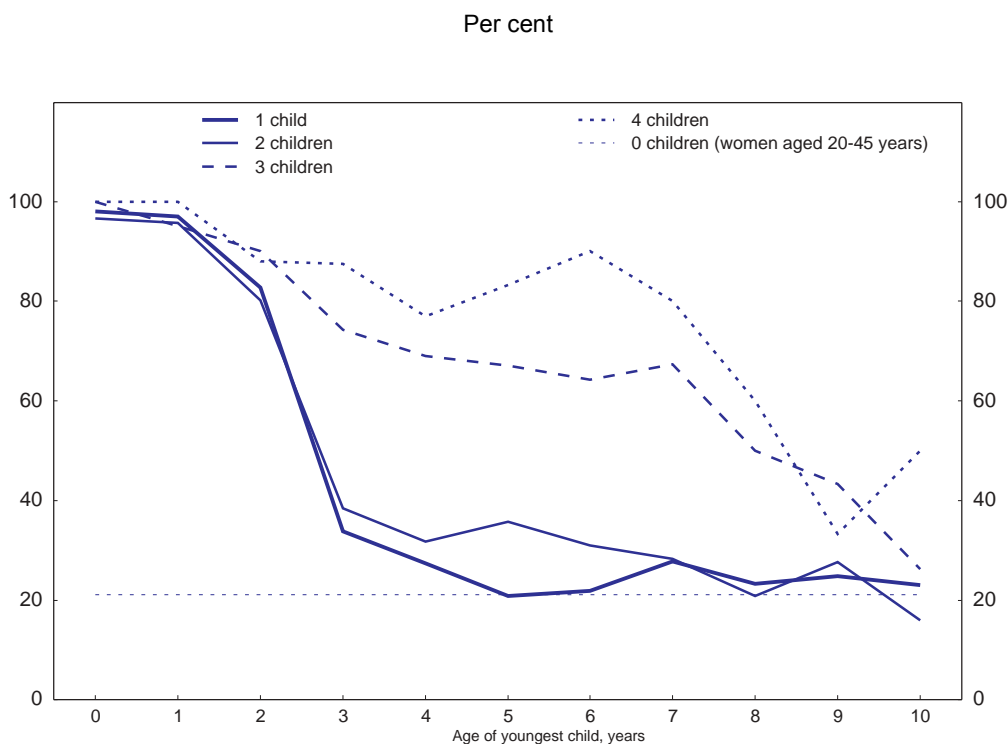


1. Employment-protected, paid leave of absence for employed parents. Maternity leave is for women at around the time of childbirth (or adoption in some countries). Additional parental leave is additional to specific maternity and paternity leave periods.

Source: OECD, Family Database.

There are relatively few public childcare places available for infants. There are legal obligations for municipalities to provide childcare services. This obligation can be fulfilled through dedicated nursery facilities (*bölcsöde*), licensed day-care centres catering for a small number of children, home care for children on an individual basis, or in some cases through running an integrated system of kindergarten and nursery. Since the early 1990s, the number of places in publicly run or supported childcare services has fallen dramatically. For instance, according to a recent OECD report, only 4% of one to two year-olds are now placed in nurseries or day-care centres (OECD, 2006). The costs of running the nurseries and other types of childcare for infants are partially covered by central-government grants and by revenues from a regulated fee for children's meals. From age three onwards, childcare and early childhood education services are comprehensive. From age three to five there is a system of kindergarten (*óvoda*), with once again only limited fee burdens for parents. Legally, children must go to kindergarten for at least one year but most children attend for the full three years.

Figure 3. Inactivity rates of mothers by the number of children<sup>1</sup>



1. Inactivity rate is  $100 \times (1 - \text{employment/population ratio})$ . Calculations are based data from the Central Statistical Office's Labour Force Survey for Q2 2005.

Source: Ministry of Finance.

Low-income families can be eligible for various forms of means-tested support. These include waivers on the fees for meals in childcare centres and kindergartens, free meals in primary and secondary schools, free textbooks and subsidised travel costs. Families can also get support to cover living costs for children in tertiary education.

## Policy needs to focus more on reconciliation between work and family life

The long leave provisions, backed by cash benefits, and the paucity of childcare services are influencing on mothers' decisions on whether (or when) to join (or return to) the labour force.<sup>3</sup> Though there is no dedicated data that tracks the employment history of women with children, the indirect evidence is compelling. Labour force survey data shows that women's inactivity rates are over 80% whilst there is at least one child aged under three in the family (Figure 3).<sup>4</sup> Furthermore, given that about 40% of birth intervals are shorter than three years and a majority of women have two children once they start a family, actual leaves in Hungary are often a lot longer than three years.<sup>5</sup>

There are several difficulties with this approach to family policy. A big risk is that the relatively small number of childcare places reflects poor supply rather than low demand, implying that some parents are being denied the opportunity to combine working while bringing up infants. From an economic perspective, very long separation from the labour market reduces women's earnings and career prospects, implying a lower employment rate and weakened human capital development at the aggregate level.<sup>6</sup> Furthermore, the policies are expensive to run. Total spending on cash benefits is relatively high, on a par with Nordic countries and much higher than peer countries, such as the Czech Republic and Slovakia (Figure 4). Given the strong need to make improvements in cost-effectiveness in all areas of public spending to help bring government deficits down, this large item of expenditure should therefore anyway come under scrutiny.

The extended leave and cash support is sometimes justified on the grounds that it encourages women to have children and is thus helping to resuscitate Hungary's low fertility rate. However, it is doubtful whether this strategy is very effective. The fertility trends shown in Figure 1 suggest the impact of these policies on the birth rate has at best been marginal; there appear to be common forces at work on fertility in east-European countries, which are having a dominant effect over any country-specific influences. Econometric evidence also suggests that the influence of cash benefits and leave allowances on fertility is relatively small and contingent on getting other areas of policy right, such as childcare (Box 2). Furthermore, any positive impact on fertility from generous leave and cash benefits is probably becoming weaker over time because the opportunity cost of taking time off work is rising due to increasing education and earnings potential.

Much greater focus on helping parents reconcile work and family life is needed. Childcare provision has to be flexible; capable of meeting current demand and changes in the volume and type of service required by parents. In addition, the right incentives structures have to be in place to encourage parents to work and this suggests a review of the core elements of family support, namely leave and family

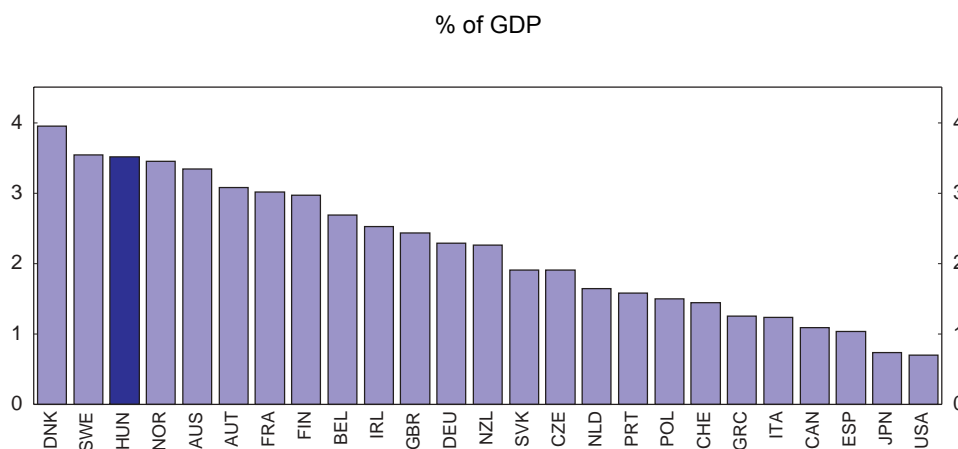
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3. The role of childcare and cash benefits on women's choices for a number of OECD countries is reviewed in the OECD's *Babies and Bosses* series (Hungary has yet to be covered in this project). The Austrian system (*Babies and Bosses, Volume 2*), for instance, has some similarity with the Hungarian system in that cash benefits and parental leave options encourage full-time parental care when children are young.
  4. In the Hungarian data only during the first months of maternity leave are women classified as being in employment. In some countries both maternity and parental leave is classified this way, making for apparently much higher activity rates.
  5. Statistics on birth intervals produced by the Hungarian Statistical Office show less than 5% of birth intervals are less than one year while a large share of intervals (about 40%) are longer than one year but less than three.
  6. A number of econometric studies have looked at the relationship between maternity leave and earnings. A study by Rhum (1998), for example, finds that the earnings of women entitled to nine months leave are 3% lower compared with when leave entitlements are only up to three months.

cash benefits, is needed. Finally, barriers to the creation of part-time jobs and other forms of work that help parents combine work and childrearing need to be removed and, more generally, employers need to be encouraged to develop family friendly work environments. The following sections discuss recent policy measures on these fronts and detail options for additional reform.

#### Box 2. Recent research on the influences on fertility

Cross-country evidence on the driving forces behind fertility by d'Addio and Mira d'Ercole (2005) underscores that cash benefits for families to have children are by no means guaranteed to have any significant impact on women's decisions on how many children they have. This is partly because there are stronger policy influences, such as the availability of childcare. This implies that achieving a balanced package can be cheaper and work better than one with ill-matched components. Also, this research on fertility underscores that there are other, more powerful, forces acting on fertility patterns. Most notably, increasing educational attainment and, linked to this, more attractive job and career opportunities for women have been depressing birth rates. This is echoed in time-series regressions on Hungarian data explaining the total fertility rate over past decades by Gal and Gabos (2005) where the coefficient relating to female employment rates is the largest among the explanatory variables. Conversely, the coefficient relating to family benefit, though statistically significant, is relatively small. This research also underscores the possibility of more complex causal connections than those implied by the regressions. For instance the authors suggest that there may be reverse causality between fertility and women's employment rates.

Figure 4. International comparison of expenditure on family support<sup>1</sup>



1. Includes family allowances, parental leave and home-help services and is for 2003.

Source: OECD (2006), Social Expenditure Database.

#### *Promoting flexible supply responses in public childcare*

The very low use of public childcare is plausibly due, in part, to weak demand. Because remaining at home to care for infants has been made relatively attractive, this is likely to have reduced the demand for childcare places. However, a number of factors point to inadequate supply. Several theoretical arguments suggest there may be under provision of childcare services. There can be free-rider problems because municipalities may have to accept children from neighbouring local authorities. Also, negative externalities can arise if the returns to childcare in terms of education and social cohesion are felt outside local community. In addition, local democracies may simply not work very effectively in this instance, such that the voters' demand for childcare do not get appropriately factored into local decision makers'

policies. In terms of evidence of under provision, the low number of places, particularly in rural areas is telling. For instance there are only about 50 childcare facilities among the very large number of small municipalities.<sup>7</sup> There are also reports of long waiting lists for childcare places.

Under provision of childcare limits families' options for combining work and family, but it also contributes to social disadvantage, notably for the Roma population. Lack of access to childcare for infants from poor backgrounds is thought to contribute to problems further down the track, such as non-attendance in kindergarten. Overall, there look to be strong returns to measures that improve municipalities' response to demand for childcare and cater for changing requirements in the type of service offered.

Central government has already stepped up pressure on municipalities to provide services. A regulation requiring localities with a population of more than 10 000 to provide nurseries (*bölcsöde*) was introduced in 2005. Financial support has also been boosted through a significant increase in central-government grants to municipalities for childcare services.<sup>8</sup> Nevertheless, the Ministry of Social Affairs and Labour estimates these grants still only cover about 50% of the costs of running services. According to a recent OECD report, the fees for meals mean that parents effectively pay for about 10-15% of the costs; implying 35-40% is covered by municipalities (OECD, 2006).

Central government should continue to work on providing regulatory pressures and improved incentives for childcare services. Reforms should focus on:

- Continued attention to provision requirements. The impact of the changes in provision regulations should be monitored and, if necessary, bolstered by further measures to increase supply. In terms of service flexibility, an increasing number of childcare centres are reportedly catering for a wider variety of working arrangements on a voluntary basis. Nevertheless, policy goals laid out in the government's programme (Government of Hungary, 2006) to encourage more flexible services should be followed up. The plan to encourage longer operating hours of childcare facilities looks particularly promising.
- Reduction in the municipalities' contribution to costs. Further increases in the central-government grant for childcare services could be considered if savings can be found elsewhere in the system – reductions in family cash benefits is one candidate (see below). The restrictions on fees could also be lightened. The typical fee for meals is around HUF 6 000 per month. This is low compared with other countries. The fees are equivalent to only about 5% of average-production-worker (APW) earnings while in most OECD countries the fees are equivalent to at least 10% of APW earnings and over 20% in several countries (Immervoll and Barber, 2005). If fees were de-regulated, the current system of waivers (or a similar mechanism) would clearly have to be retained to ensure access for low-income households.

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7. This figure is taken from Hungarian Central Statistical Office (2002). This publication also illustrates the wide disparities in the supply of childcare places between urban and rural areas. For instance, the statistics show there are roughly 20 childcare places per 100 children aged 0 to 2 years in Budapest while in villages there is, on average, only one place per hundred children.

8. There has been a 50% increase in the per-child grant for nurseries and a 250% increase in the grants for family day-care between 2004 and 2007. In 2007 the per child central-government grant is HUF 547 000 for nurseries and HUF 250 000 for family day-care.

- More radically, a voucher system could be considered. At present, competition and diversity in childcare services is weak because subsidies are channelled into either direct provision or providers chosen by the local authority, and fees are regulated. A system for childcare in which vouchers are given to parents to spend on childcare services (possibly in lieu of cash benefit) could be one way of widening provision and allowing the distribution of central-government resources to more strongly reflect parental preferences.

### ***Improving the system of initial financial support and leave allowances***

The Hungarian government considers the system of long parental leave allowances and associated cash benefits reflects societal choices for family-based childcare and has no plans for significant change. However, given the high level of spending on cash benefits, the adverse effects on women's careers of long career breaks and the questionable impact on fertility, reforms should be considered. Specifically, options for reducing the duration of leave and benefit provisions should be explored and savings from this channelled into boosting childcare services. A wide range of alternative adjustment packages could be devised to reform the system, but the following common elements should be considered:

- Removal of the GYET benefit. From the childcare perspective, GYET is somewhat superfluous because it comes on stream after all the children have reached an age when they can attend kindergarten. If the financial support from GYET is considered important, it could be replaced by an increase in the per-child family allowance.
- Significant reform of the GYES and GYED benefits. The insurance benefit GYED is currently designed as a purely "stay at home" incentive as women are only eligible if they remain off work and they are not even supposed to claim the benefit if they put their children in childcare. GYES, with the new rules that allow women to work and claim benefit, does not have this problem. But it does pay out indiscriminately to all families with infants no matter whether the mother has any demonstrable opportunity cost in being a full-time child carer. One way forward would be to introduce vouchers for childcare as discussed above.
- Whatever specific changes are considered, possibilities for extended leave ought to be cut back and savings should sought to help fund increased support for childcare services. Looking at Figure 2, a combined maximum length of maternity and parental leave of 12 months, for example, would bring Hungary in line with the norm for a number of other OECD countries. The advantage of keeping maximum paid leave entitlements to one year or less is that overlapping leaves are less likely.

These suggested measures imply radical change to the amount of benefit and length of leave allowances. Indeed, if all extensions to leave were cut then Hungary would swing from having one of the longest leave entitlements to among the shortest. Therefore, some offsetting measures could be built into a reform package. Two possible routes are:

- Increases in the replacement rate (and perhaps raising of the cap) of the insurance benefit covering standard maternity leave (TGYAS).
- Increased paternity leave. In principle, fathers (and other grandparents) can claim GYES or GYED benefit (and the associated leave entitlements) instead of the mother, thus allowing for some flexibility in the organisation of childcare within families. However, provisions for fathers to take leave in the first months following the birth of the child ("paternity leave") are relatively limited (fathers can take up to five days leave in the two months following the birth of each

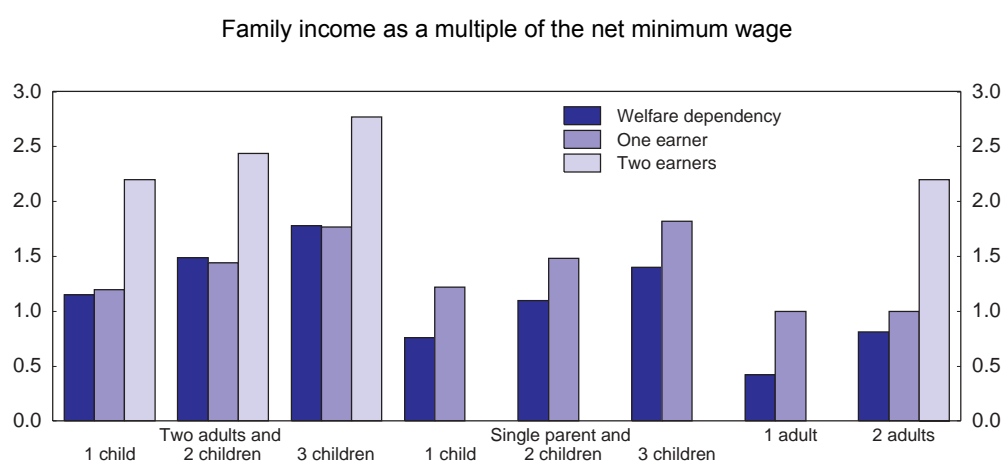
child). A number of OECD countries have sought to help families combine work and childcare by increasing paternity leave entitlements. For instance Belgium, Denmark and Finland allow up to 2-3 weeks paternity leave while in Norway and Sweden as many as 6 weeks can be taken (OECD, 2006).

### *Dealing with welfare traps*

As discussed earlier, Hungary's low employment rate means a sizeable minority of households are fully dependent on welfare payouts. The new system of social assistance makes for a more stable income through top-up payments but it does not solve, and may indeed have deepened, welfare traps. There are some provisions to prevent the welfare system from making work financially unattractive. If someone in a welfare-dependent household gets a job, the household receives 50% of the previous top-up payment for the first three months and then 25% for the following three months. After six months, the top-up is withdrawn completely. Though this is better than an immediate 100% withdrawal of benefit, the provision is unlikely to have much influence on families looking at the long-term returns to working.

Simulation results suggest there is indeed little incentive to work once the longer-term situation is considered, particularly given that welfare-dependent households are likely to get only low-wage job offers. This is illustrated in Figure 5 that shows the incomes of households in three situations: one where nobody works, another where one person has a minimum-wage job and a third where two people have minimum-wage jobs. In terms of family benefits the calculations only include family allowances, in other words the scenario represents the situation after children start kindergarten, a time when parents are likely to contemplate entering the labour force. As can be seen the welfare trap is deepest when only one parent works; family income in this instance is virtually the same as when neither parent works.

Figure 5. The welfare trap problem



Note: The scenarios assume earners are on the minimum wage. The calculations factor in the minimum family income guaranteed in the top-up system.

Source: OECD calculations.



The welfare-trap problem could be tackled on two fronts:

- Alteration of the weighting system used in calculating the “social welfare guarantee”. The weights used in the equivalence scale are somewhat higher than those used in other OECD countries. The weight of 0.9 for the second (and subsequent) adult in a household is higher than used elsewhere, as are the weights of 0.8 for each of the first two children and 0.7 for third and subsequent children (see Box 3).
- Extension of the period allowing retention of a share of the welfare top-up payments when someone gets a job. More radically, earned-income tax credits could be introduced to increase the returns to a single-earner household.

Welfare trap problems aside, the new top-up system may well suffer from targeting problems and this issue needs to be carefully monitored and dealt with as appropriate. Some Hungarian policymakers are sceptical about means-tested benefits in general because of low take-up rates among genuinely needy households and possibilities of abuse due to underreporting of earnings and undeclared in-kind forms of income. Reportedly, these problems are amplified by inadequate administrative structures for means testing.

There also appear to be targeting problems in housing support schemes. Research by the Ministry of Finance cites evidence that housing support does not reach many who are genuinely needy, and that comparatively well off households are among the main beneficiaries (Benedek *et al.*, 2006). Fortunately, the sums involved are not large and so the wastage is not significant in a fiscal sense, nor is the support likely to be distorting household behaviour. Nevertheless, this issue ought to be on the list of priorities in welfare reform.

The various means-tested waivers of education costs can potentially aggravate the welfare traps by further narrowing the gap between effective family income under full welfare dependency and that when one or both parents work. However, there has recently been considerable widening of the waivers, which should reduce this problem. The Ministry of Education has increased access to free textbooks in the 2006-07 school year and over half of students are expected to be covered. Eligibility for discounted or free meals has also been widened.

### Box 3. The debate about east-European equivalence scales

The equivalence scales used by east-European countries in benefit formula such as Hungary's top-up welfare payments tend to use higher weights than in other OECD countries. For example, international comparisons of living standards and poverty commonly use the “modified OECD scale” which attaches a weight of only 0.5 to additional family members. Part of the reason for the high east-European weights is purely historical; relatively generous weighting scales were a feature of the pre-1990s socialist regimes and either inattention to the issue or political difficulties in reducing the weights have prevented reform. But there are technical reasons why higher weights may be appropriate for east-European countries:

- High rates of home ownership imply the differences in equivalence scale weights for family members should be narrower than elsewhere. Full home ownership (*i.e.* without outstanding loans) is common, even among low-income households. Hence, accommodation costs typically do not feature in household living expenses. Because housing is a key source of scale-economies in spending, this implies differences in weights across family members should be narrower in eastern-European countries compared to countries where low-income households pay rent or have housing loan repayments. However, this also implies that the overall generosity of safety-net transfers ought to be lower in east-European countries than elsewhere because housing costs do not have to be covered.
- The relatively low GDP per capita of east-European countries means households spend a lower share of their incomes on consumer durables and more on items, such as food, where economies of scale are weaker. This again suggests the gaps between equivalence scale weights should be relatively narrow. But this also implies that the gaps should be widened over time as these countries catch-up with living standards and spending patterns elsewhere.

### *Avenues for further simplification*

With eight schemes of long and short-term financial support, the system of cash benefits could do with some further simplification. Indeed, three schemes could be scrapped without any significant implications for either the universal or targeted “safety net” dimensions of policy:

- With the introduction of the social welfare guarantee in June 2006, the cash component of “child social support” scheme is now effectively redundant and has anyway been reduced to relatively small biannual payments.
- The maternity grant makes only a small contribution to the total value of financial support. As such, the grant represents unnecessary clutter in family policy and could be factored into one of the other benefits, such as the family allowance.
- The third-child tax allowance – the only allowance remaining following the changes made in January 2006 – could also be scrapped. If deemed necessary this move could be compensated by an adjustment of family allowances.

### *Encouraging the creation of family-friendly jobs and work environments*

The government has recently implemented, or is planning, a range of active measures that focus on encouraging employers to take on working parents and to develop family friendly work environments. Most notably, under the Start Plus programme, as of July 2007 significant reductions in social contributions will be available to employers taking on parents who are receiving the GYES benefit, or whose GYES, GYED or GYET benefit has recently expired. Past initiatives have included the introduction of an annual award (the *Family-Friendly Workplace Award*) to companies and institutions implementing outstanding family-friendly measures and the preparation of a handbook on creating family friendly workplaces as part of an EU sponsored project. Further research on good practice is underway. In addition, some EU Structural Funds are being allocated to support training and other services that help women return to the labour market or to set up businesses, and to disseminate information on creating family-friendly work environments.<sup>9</sup>

The government is also using its role as an employer to promote family friendly working arrangements with the introduction of provisions for working from home for central-government employees. Further reforms that give more flexible choices to public-sector employees would not only directly affect a large number of workers but also provide a lead for changes in working arrangements elsewhere.

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9. Plans to use Structural Funds to support the labour market participation of women are outlined in Section 5.5 of the *National Development Plan of Hungary 2004-2006* and similar proposals are made in the *2007-2013 Plan*. Six working groups have been set up to implement the European Commission’s Roadmap for Equality between Women and Men 2006-2010, and another working group is dealing with the question of wage inequalities.

In addition to active measures, the authorities should seek to remove barriers that may be preventing the creation of jobs that can more easily be combined with childcare. In Hungary the market for part-time and other non-standard working arrangements is small.<sup>10</sup> One reason for this could be that the leave entitlements have so far meant little demand for such jobs. The lump-sum healthcare contribution is also thought to have dissuaded the creation of short-hours jobs. The final phase-out of the contribution is on hold as part of the government's austerity package. However, when fiscal room allows some tax reduction, resumption of the phase out ought to be given priority.

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10. Less than 5% of employees in Hungary have jobs involving fewer than 30 work hours per week. In most OECD countries the share is at least 10% and in many it is over 20%.

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## ANNEX A1

DETAILS OF FAMILY SUPPORT<sup>1</sup>

## Long-term financial support for families (benefit amounts as of 2006)

	Duration and nature of benefit	Benefit amount	Other considerations
<b>Family allowance</b> ( <i>Családi pótlék</i> )	Universal benefit for each child up to completion of secondary education (with an age limit of 23).	Two-parents families (monthly amounts per child): One child, HUF 11 000; Two children, HUF 12 000; Three or more children, HUF 14 000. Single parents: One child, HUF 12 000; Two children, HUF 13 000; Three or more children, HUF 15 000.	The allowance is not counted as taxable income and no other deductions are made (such as pension contribution).  A 13 <sup>th</sup> month payment was abolished in January 2006.  When children are no longer eligible, the per-child allowance is not reduced for younger siblings.
<b>Family tax credit</b> ( <i>Családi adókedvezmény</i> )	Available to families with three or more children. The age limits are the same as for the family allowance.	HUF 4 000 per month per child. The credit can be split between both parents but it is non-refundable.	Tax credits for families with one or two children were scrapped in January 2006.
<b>Child social support</b> ( <i>Rendszeres gyermekvédelmi kedvezmény</i> )	<i>Per capita</i> household income must be below 120% of the minimum old-age pension (130% for single parents).	Biannual payments of 5 000 HUF (in July and in November).  Support also entails various in-kind benefits.	This scheme replaced a more generous system of monthly means-tested child protection support in January 2006.
<b>Supplementary child social support</b> ( <i>Kiegészítő gyermekvédelmi támogatás</i> )	Only guardian's (e.g. grandparents) of children who are receiving Child Social Support are eligible.	22% of the minimum old-age pension per month per child, plus biannual payments of HUF 7 500 (in July and in November).	The scheme was introduced in April 2006.
<b>Guaranteed social minimum</b> ( <i>Rendszeres szociális segély</i> )	A top-up payment that brings family income up to a specified level.  The applicant must not be employed and typically must agree to engage in certain activation measures. This requirement does not apply to those with disabilities.	A multiple (the "per capita equivalent") of 90% of the minimum monthly pension based on the following scale: 1 for first adult 0.9 for second (or other) adults 0.8 for each of the first two children 0.7 for the third and subsequent children (each).	This system was introduced in June 2006.  If the claimant gets a job, the family gets 50% of the previous top-up payment for the first three months and 25% for the following three months.
<b>Home maintenance support</b> ( <i>Lakásfenntartási támogatás</i> )	Two means-tested schemes operate, one centrally defined and one locally defined. Both are administered locally.	Eligibility is based on per capita income and the size of the apartment or house.  Some benefits are in-kind (for example, rent-free or reduced-rent accommodation).	Payout amounts are not typically very large. For example, a household budget survey by the Hungarian statistical office for 2003 puts the average value of support at about HUF 3 800 per recipient household.

**Additional financial support for the first years of parenthood (benefit amounts as of 2006)**

	<b>Duration and nature of benefit</b>	<b>Benefit amount</b>	<b>Other considerations</b>
<b>Maternity grant</b> ( <i>Anyasági támogatás</i> )	One-off payment at birth.	225% of the monthly minimum pension.	Not counted as taxable income.
<b>Pregnancy and confinement benefit</b> ( <i>Terhességi gyermekágyi segély, TGYAS</i> ).	Payable up to 24 weeks and designed to cover statutory maternity leave).  Eligibility requires claimant is insured. Insurance requires 180 days contributions over the previous two years. Time spent in secondary and tertiary education count.	70% of daily average <i>gross</i> earnings over the 180 days prior to the birth of the child. If another child is born before the mother goes back to work then there is a ceiling to the benefit of 70% of twice the minimum wage.	Not eligible if the claimant has any other form of income (with exception of the family allowance).  The benefit is taxable and the pension contribution (8.5%) is deducted.
<b>Childcare benefit</b> ( <i>Gyermekgondozási díj, GYED</i> ).	Available from end of pregnancy and confinement benefit until the child reaches two years of age.  Eligibility requires claimant is insured (as for TYGAS).	Same benefit level as TGYAS, except that the ceiling of 70% of twice the minimum wage always applies.  The benefit can be paid to fathers instead of the mother.	Subject to the same conditions regarding other forms of income as TYGAS.  The claimant is not eligible if they put their child in nursery school.  Taxable but the pension contribution (8.5%) is deducted.
<b>Childcare allowance</b> ( <i>Gyermekgondozási segély, GYES</i> )	Available from birth of child until aged three years.	The value of the minimum old-age pension (HUF 25 800) per child.  The benefit can be paid to fathers or grandparents instead of the mother.	As of January 2006 once the child is 1 year old claimants can work full time with no loss of benefit (previously the claimant could only up to 20 hours per week and remain eligible).  Not taxed if there are no earnings but pension contribution (8.5%) is deducted. The benefit is included in taxable income if any earnings are claimed.
<b>Child raising support</b> ( <i>Gyermeknevelési támogatás, GYET</i> ).	Available to families where there are three or more children and the youngest is aged between 3 and 8 years.	The value of the minimum old-age pension (HUF 25 800).	Same as GYES.

## Other forms of support for families

<b>Medical care</b>	<ul style="list-style-type: none"> <li>▪ Pregnancy and childbirth as well as children's medical care are covered by the state. In the plans for a tiered healthcare system formulated following the 2006 general election, medical care associated with childbirth and children would have universal coverage. There are no special waivers on fees for prescription drugs for children. There are no significant barriers to establishing private clinic services for pregnancy and childbirth.</li> </ul>
<b>Maternity, paternity and parental leave</b>	<ul style="list-style-type: none"> <li>▪ Maternity leave is 24 weeks and is typically taken from 4 weeks before childbirth until 20 weeks after (a minimum of 6 weeks must be taken). Employers must place those returning to work back in their original post, or an equivalent position, and at same pay grade (or higher).</li> <li>▪ Paternity leave of 5 days can be taken within the first two months after childbirth.</li> <li>▪ Claimants to either GYES or GYED benefit (but not GYET) are entitled to leave from their employer with the same rights as under maternity leave.</li> <li>▪ Two supplementary days annual holiday for one child aged under 16, four days for two children and 7 days for more than two children.</li> <li>▪ During the first 6 months of nursing a working mother is entitled to an extra hour off work, twice a day, followed by one hour off until the ninth month.</li> </ul>
<b>Childcare centres and kindergarten</b>	<p>Childcare centres</p> <ul style="list-style-type: none"> <li>▪ There are legal obligations for municipalities to provide childcare for pre-kindergarten age children (<i>i.e.</i> aged under 3 years). As of 2005 there are also requirements that municipalities with populations over 10 000 have to set up nurseries (<i>bölcsöde</i>) which typically have 20 to 100 places. Otherwise, childcare services typically take the form of smaller day-care centres catering for up to 7 children, or through the employment of child carers to run day-care or help families on an individual basis. The day-care centres can be run from private homes or by non-governmental organisations.</li> <li>▪ Childcare facilities are typically open 8-10 hours per day and close in the summer for 4 to 5 weeks. Working parents usually get priority in the allocation of places. Service quality is maintained by a system of licences, a register of childcare experts and by external checks and evaluations.</li> </ul> <p>Kindergarten</p> <ul style="list-style-type: none"> <li>▪ One year of kindergarten (<i>óvoda</i>) covering ages 3 to 5 is compulsory (most children are in fact sent for the full three years), municipalities are responsible for provision and get state financial support for this (provision rules are lighter for small communities). The Ministry of Education is responsible for overall regulation and policymaking. Kindergartens are open 10 hours per day for 50 weeks of the year.</li> </ul> <p>Fees</p> <ul style="list-style-type: none"> <li>▪ For both kindergarten and day-care there are only fees for meals (indeed, the local authorities are not allowed to charge any other type of fee). Children from families getting the "child protection support" are exempted and families with three or more children get a 50% reduction.</li> </ul> <p>Quality assurance</p> <ul style="list-style-type: none"> <li>▪ A uniform system of quality assurance applies to both public and private providers of childcare and includes regulations on carers' qualifications and a system of licensing involving annual checks on services.</li> </ul>
<b>Primary and secondary schooling</b>	<ul style="list-style-type: none"> <li>▪ Available free-of-charge in state schools. Private schools (relatively small in number) are subsidised by the state.</li> <li>▪ Schools must provide after-school supervision for students up to age 12.</li> <li>▪ School meals, text books and travel costs are provided free of charge, subject to means-testing.</li> </ul>
<b>Tertiary schooling</b>	<ul style="list-style-type: none"> <li>▪ The state subsidises tuition costs in public universities.</li> <li>▪ Support for student living expenses is available based on family income. Indirect subsidy is also <i>via</i> state-supported loans.</li> </ul>

1. The tables describe the system in place in 2006 and aims to show the support available for the large majority of households. Notably, details of additional financial support for disabled children are not included.

## ANNEX A2

### THE INFLUENCE OF CASH BENEFITS ON FAMILY INCOME

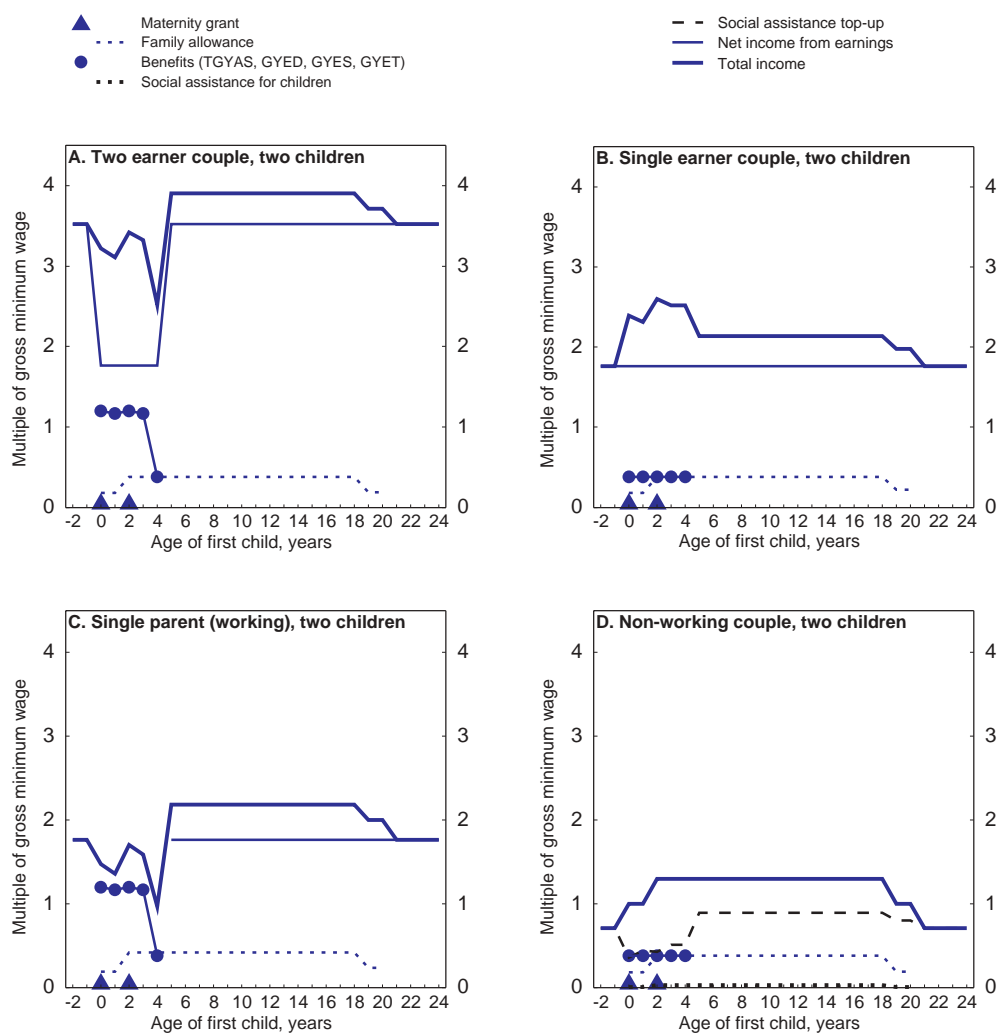
To illustrate how the system of family benefits works, Figure A2.1 shows the components of family income under various scenarios. All the scenarios assume children are born two years apart (approximately the median birth interval), that full use is made of available benefits and leave options and that earners are on the average wage (an estimated figure of HUF 110 000, net, per month is used). To provide a metric, all components of income are expressed in multiples of the gross minimum wage (HUF 62 500 in 2006).

The first panel of Figure A2.1 shows the income of a working couple who have two children. First off, the family gets the universal maternity grant with the birth of each child. More importantly, family allowance payments also begin at the birth of the first child and increase when the second child is born. On top of this, for the first six months after the birth of each child the women gets the earnings-related TGYAS benefit and this is followed up by the second component of insurance benefit, GYED, which lasts until both children are at least two years old. After GYED expires, the family is eligible for one year of GYES benefit because the youngest child is not yet three years old. When both children are over three (and eligible to go to kindergarten), the mother is assumed to return to work (leave has totalled 5 years) and the family allowance is the only benefit.

The second panel of Figure A2.1 illustrates the case of a single-earner couple, the second most common form of household. The mother is assumed to have not worked before starting a family and does not enter the labour force when the children start school. The main difference with the two-earner couple is that additional financial support for the early years comes from the GYES benefit only – this lasting from the birth of the first child until the second child reaches kindergarten age (five years in this scenario). The third panel shows a scenario for a working single parent. The structure of benefits and length of leave is the same as for the working couple, but the family allowances are higher. The fourth panel illustrates the case of a welfare dependent couple with two children. On top of the universal maternity grant, family allowance and GYES benefit, the family gets biannual social support payments. However, the most important influence on family income is the top-up under the new social guarantee.



Figure A2.1. Family incomes: some illustrative scenarios



Source: OECD calculations.

## ANNEX A3

## IMPACT OF THE JANUARY 2006 CHANGES TO FINANCIAL SUPPORT FOR FAMILIES

In January 2006 the per child family allowances were increased significantly but at the same time several cuts in financial support were made: a 13<sup>th</sup> month family allowance payment was scrapped, tax allowances were removed (except for when families have a third child) and child social-security support was cut back from monthly payments to a relatively small biannual payment.

The table below illustrates the impact of these changes by comparing the value of benefits in January 2005 with those in January 2006. As can be seen the impact on the total value of benefit is relatively small.

Comparison of family support between 2005 and 2006

All benefit amounts in HUF 000 per month	Number of children		
	1	2	3
<i>Example 1:</i> Very low income family (family allowance plus child protection support but no tax credit)			
Value of support January 2005	10.9	24.2	41.6
Value of support January 2006	11.8	25.7	44.5
Difference	0.9	1.4	3.0
<i>Example 2:</i> Other families (family allowance plus tax credit but no child protection support)			
Value of support January 2005	8.5	21.4	55.4
Value of support January 2006	11.0	24.0	54.0
Difference	2.5	2.6	-1.3

Source: OECD.

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